In the Supreme Court of the United States

OCTOBER TERM, 1956

No. 1010

ANGELA MACEVOY WOODLAW, OTIS G. JAMES AND STEPHEN W. MATTHIESU, EXECUTORS OF THE ESTATE OF G. T. WOODLAW, DECEASED, PETITIONERS

v.

HUGH H. EARLE, FORMER COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF OREGON

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The District Court rendered no opinion.[1] The opinion of the Court of Appeals (Pet. 13–42) is not reported.

JURISDICTION

The judgment of the Court of Appeals was entered on February 28, 1957. (R. 155.) An order denying petition for rehearing was entered on April 10, 1957. (R. 156.) The petition for a writ of cer-

[1] The District Court's findings of fact and conclusions of law appear at R. 41–51, 128–129.

tiorari was filed on May 18, 1957. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254.

QUESTIONS PRESENTED

1. Whether the Court of Appeals properly concluded that the payments here involved were corporate distributions equivalent to a taxable dividend within the meaning of Section 115 (g) of the Internal Revenue Code of 1939.

2. Whether the Court of Appeals erred in considering evidence which was part of the record on appeal but was not contained in the printed record.

STATUTE AND OTHER AUTHORITIES INVOLVED

The pertinent provisions of the statute and other authorities involved are Section 115 (a), (b), (c), (g) and (i) of the Internal Revenue Code of 1939; Section 29.115-9 of Treasury Regulations 111; S. Rep. No. 52, 69th Cong., 1st Sess., p. 15; and Rules 10 and 17 of the Rules of the United States Court of Appeals for the Ninth Circuit. They are set forth in the Appendix, *infra*, pp. 11–16.

STATEMENT

The pertinent facts as found by the District Court in its original findings of fact (R. 41–51) and in its additional findings of fact (R. 128–129) are as follows:

Petitioners here are the executors of the estate of G. T. Woodlaw, deceased. With the exception of qualifying shares, Woodlaw owned all of the stock of the Woodlaw Investment Company, an Oregon

Corporation organized on April 15, 1920. During 1946, Woodlaw sold 1,400 shares of his stock to this company and in reporting the sale on his 1946 income tax return treated the proceeds as a capital gain to the extent that such proceeds exceeded par value of the stock. (R. 44, 128.)

The consideration for the above sale was $266,000, which was paid by the company to Woodlaw in the following manner: (1) cash in the amount of $163,000 paid in 1946, in the amount of $2,000 paid in 1947 and in the amount of $370.90 paid in 1949; (2) settlement in 1946 of debts due from Woodlaw in the amount of $40,225.15 and carried in an open account for the years 1930, 1931, 1932, 1939, 1940, and 1944; and (3) transfer in 1949 of a contract receivable valued at $60,403.95. (R. 44–45, 48–49.) For items making up the sum of $40,225.15 owed by Woodlaw, see R. 46–47, 49.

The Woodlaw Investment Company kept its books and made its tax returns on the cash basis. It had substantial undistributed profits and its surplus account as shown on its 1946 return is as follows (R. 48):

Beginning Surplus		$286,985.99
Profit for year 1946		35,357.15
Total		322,343.14
Deduct Federal Income Tax Paid	$15,294.22	
Note Receivable Cancelled	1,000.00	
Income taxes 1946 (United States)	8,339.29	
Income taxes 1946 (State of Ore.)	3,215.07	27,848.58
Balance		294,494.56

For the years 1929 through 1949, the tax returns of Woodlaw Investment Company showed the following (R. 128–129):

Year	Net income	Earned surplus and Undivided profits	Dividends paid
1929		$114,013.22	
1930	$41,023.09	151,488.38	None
1931	23,889.86	170,294.38	None reported
1932	6,505.69	173,419.29	None
1933	9,708.71	191,030.47	None
1934	1,391.51	197,595.22	None
1935	(20,721.29)	159,683.77	None
1936	(1,910.12)	158,298.32	None
1937	5,149.90	164,022.89	None
1938	(14,905.29)	144,219.14	$5,241.60
1939	6,202.06	146,239.89	5,000.00
1940	10,330.00	156,351.67	None
1941	21,122.65	173,985.92	None
1942	26,902.84	195,495.91	None
1943	23,840.10	212,297.18	None
1944	31,867.68	229,551.12	None
1945	59,377.47	286,985.99	None
1946	35,357.15	180,043.92	None
1947	26,758.78	198,468.41	None
1948	30,730.73	222,651.98	None
1949	59,536.75	270,423.64	None

The Woodlaw Investment Company has been primarily engaged in the business of owning, leasing and renting of real estate in Portland, Oregon. (R. 48). It has not only continued in existence up to "the present time" but has also continued in the same type of business. (R. 129.)

On October 12, 1945, the Woodlaw Investment Company sold its Gerlinger Building and on May 29, 1946, its Hamilton Building. It also sold some undeveloped lots in 1946. (R. 48.)

On the basis of the foregoing facts, the District Court found (R. 50):

> That the transaction wherein G. T. Woodlaw, deceased, received in the year 1946, $163,000.00 for 1,400 shares of the capital stock of Woodlaw Investment Co. together with the additional sum of $2,000.00 in the year 1947 and

> a real estate sales contract in the year 1949 with a balance due of $60,403.95 with additional cash in that year in the amount of $370.90 was not a transaction equivalent to the distribution of a taxable dividend within the meaning of Section 115 (g) of the Internal Revenue Code. The net effect of the distribution to the said G. T. Woodlaw was a distribution of capital assets.

The District Court further found (R. 50):

> That there was in existence at the time of the transaction in 1946 involving the sale of the stock by the decedent, G. T. Woodlaw, to Woodlaw Investment Co. a legitimate business purpose therefor and Section 115 (g) of the Revenue Act is inapplicable.

Upon the above findings, the District Court concluded that the petitioners here were entitled to recover deficiencies in income tax, with interest, which had been paid for the years 1946, 1947, and 1949. (R. 51.)

The Court of Appeals (Judge Fee dissenting) found the decision of the lower court clearly erroneous. (R. 151.) Accordingly, it reversed the decision but remanded the case for a clarification of the District Court's finding as to the debts cancelled in 1946. (R. 153.)

ARGUMENT

1. The Court of Appeals reversed the decision of the District Court because it concluded (R. 151) that, on "the law and facts of this case", the decision was clearly erroneous. It held that the payments involved here are equivalent to ordinary dividends and

are taxable under 1939 Code Section 115 (g) (Appendix, *infra*, p. 12), which provides that, if a corporation cancels its stock in such a manner as to make the distribution and cancellation in whole or in part essentially equivalent to a dividend, the amount so distributed shall be treated as a taxable dividend.

As the Court of Appeals pointed out (R. 136–137), the District Court's decision is based on its Findings XIX and XX (R. 50), which state (1) that the net effect of the payments was a distribution of capital assets, and (2) that there was in existence at the time of the sale of the stock by Woodlaw to the Woodlaw Investment Company a legitimate business purpose therefor.[3] The Court of Appeals correctly found that these ultimate findings (or conclusions) are wholly unsupported by evidence. The underlying facts are painstakingly recited in Judge Barnes' opinion below (Pet. 19–27) and, significantly, are not disputed in the petition (see Pet. 11). As the opinion further demonstrates (Pet. 27–38), in reaching a conclusion rested on these undisputed facts the court below applied the precise criteria which have been approved in many cases holding that payments under similar circumstances should be taxed as dividends under Section 115 (g). *Bazley* v. *Commissioner*, 155 F. 2d 237 (C. A. 3d), affirmed, 331 U. S.

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[3] Although this finding is ambiguous, we assume, *arguendo*, that it is intended to imply a business purpose on the part of the corporation, since it would certainly not aid petitioner to show that the corporation's purchase of the stock was made for reasons personally beneficial to the taxpayer-stockholder. *Smith* v. *United States*, *supra*; *Bazley* v. *Commissioner*, *supra*; see, also, *Keefe* v. *Cote*, 213 F. 2d 651, 657 (C. A. 1st).

737; *Chandler's Estate* v. *Commissioner*, 228 F. 2d 909 (C. A. 6th); *Commissioner* v. *Roberts*, 203 F. 2d 304 (C. A. 4th); *Smith* v. *United States*, 121 F. 2d 692 (C. A. 3d); *Flanagan* v. *Helvering*, 116 F. 2d 937 (C. A. D. C.); *Stein* v. *United States*, 62 F. Supp. 568 (C. Cls.); *Vesper Co.* v. *Commissioner*, 131 F. 2d 200 (C. A. 8th). Also, see Sec. 29.115–9 of Treasury Regulations 111 and S. Rep. No. 52, 69th Cong., 1st Sess., p. 15 (1939–1 Cum. Bull. (Part 2) 332, 344) (Appendix, *infra*, pp. 12–14).[4]

As to the alleged business purpose for the payments to Woodlaw, examination reveals that none of the District Court's findings (R. 41–51) explains what or whose business purpose it was, and none indicates that the Woodlaw Investment Company intended to liquidate or had any plans for contraction of its business. Nor is there anything in the corporate minutes (R. 100–101) on the subject of liquidation. Indeed, the minutes relative to the purchase of Woodlaw's stock in 1946 are entirely silent as to the purpose of such purchase or the resulting payments. Moreover, although Woodlaw's attorney and his widow showed by their testimony that they were well informed as to his business, neither indicated that the sale of stock

[4] Petitioner contends (Pet. 3, 12) that these criteria have been invoked, without exception, in cases in which the trial court's determination was sustained. This is not so, as *Commissioner* v. *Roberts*, *supra*, illustrates. In all events, it needs no argument that the criteria which are meaningful for purposes of determining the justifiability of an ultimate finding as to the nature of a transaction are also pertinent—and necessarily so—for purposes of determining whether such a finding is *un*justified.

was in any way connected with a purpose to liquidate holdings. (R. 78–83, 103–120.)

Additional facts which were affirmatively found by the District Court and are contrary to its conclusion that the payments were a distribution of capital assets include the following: (1) after the 1946 transaction, the Woodlaw Investment Company not only continued in existence, but engaged in the same type of business down to "the present time" (*i. e.*, October 18, 1955) (R. 129); (2) in the twenty-one years from 1929 through 1949, dividends were paid only in 1938 and 1939, although, during all of that period, the company had a large accumulation of earned surplus and undivided profits available for dividends, having enjoyed net income in every year except 1935, 1936, and 1938 (R. 129); and (3) after the sale and retirement of part of Woodlaw's stock in 1946, he still held the same proportion of the stock and as sole stockholder (except for qualifying shares) was still in control (R. 44). In view of these primary findings and the absence of subsidiary findings which would point in a contrary direction, the Court of Appeals was amply warranted in holding a "definite and firm conviction that a mistake has been committed." *United States* v. *Gypsum Co.*, 333 U. S. 364, 395.

2. Petitioner complains that the Court of Appeals considered evidence that was not included in the printed record, although it was, as petitioner concedes (Pet. 7), part of the record on appeal. It is urged that the court thus violated its own Rule 17 (Appendix, *infra*, pp. 15–16), which provides in sub-

stance that the court will only consider the printed portions of the record.

Such a rule is, of course, designed to impose upon counsel a burden of care in designating matter for printing. But since rules of practice have as their ultimate objects the promotion of justice and the facilitation of the business of the courts (*Hormel* v. *Helvering*, 312 U. S. 552, 557), it has never been doubted that a court may withhold a sanction which its rules would permit it to impose. *United States* v. *Breitling*, 20 How. 252, 254.

Here, there is no basis whatever for a claim of prejudice. The only items from the unprinted record to which the court referred were Woodlaw's Last Will and Testament written in 1948 (which contemplated the continued existence of the Woodlaw Investment Company, see Pet. 26) and evidence of the increased value of the remaining shares of Woodlaw Investment following the retirement of the 1,400 shares in 1946 (see Pet. 29). Far from introducing unsuspected elements into the processes of appellate deliberation, these items of evidence appearing in the unprinted record on appeal merely served to corroborate the primary findings of the District Court summarized above (p. 8).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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JUNE 1957.

APPENDIX

Internal Revenue Code of 1939:

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

(a) [as amended by Sec. 166 of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Definition of Dividend.*—The term "dividend" when used in this chapter (except in section 201 (c) (5), section 204 (c) (11) and section 207 (a) (2) and (b) (3) (where the reference is to dividends of insurance companies paid to policy holders)) means any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made.

(b) *Source of Distributions.*—For the purposes of this chapter every distribution is made out of earnings or profits to the extent thereof, and from the most recently accumulated earnings or profits. * * *

(c) [as amended by Sec. 147 of the Revenue Act of 1942, *supra*] *Distributions in Liquidation.*—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent pro-

vided in section 112. In the case of amounts distributed (whether before January 1, 1939, or on or after such date) in partial liquidation (other than a distribution to which the provisions of subsection (h) of this section are applicable) the part of such distribution which is properly chargeable to capital account shall not be considered a distribution of earnings or profits. * * *

* * * * *

(g) *Redemption of Stock.*—If a corporation cancels or redeems its stock (whether or not such stock was issued as a stock dividend) at such time and in such manner as to make the distribution and cancellation or redemption in whole or in part essentially equivalent to the distribution of a taxable dividend, the amount so distributed in redemption or cancellation of the stock, to the extent that it represents a distribution of earnings or profits accumulated after February 28, 1913, shall be treated as a taxable dividend.

* * * * *

(i) *Definition of Partial Liquidation.*—As used in this section the term "amounts distributed in partial liquidation" means a distribution by a corporation in complete cancellation or redemption of a part of its stock, or one of a series of distributions in complete cancellation or redemption of all or a portion of its stock.

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(26 U. S. C. 1952 ed., Sec. 115.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

SEC. 29.115-9. *Distribution in Redemption or Cancellation of Stock Taxable as a Dividend.*—If a corporation cancels or redeems its stock (whether or not such stock was issued as a stock dividend) at such time and in such manner as to make the distribution and can-

cellation or redemption in whole or in part essentially equivalent to the distribution of a taxable dividend, the amount so distributed in redemption or cancellation of the stock, to the extent that it represents a distribution of earnings or profits accumulated after February 28, 1913, shall be treated as a taxable dividend.

The question whether a distribution in connection with a cancellation or redemption of stock is essentially equivalent to the distribution of a taxable dividend depends upon the circumstances of each case. A cancellation or redemption by a corporation of a portion of its stock pro rata among all the shareholders will generally be considered as effecting a distribution essentially equivalent to a dividend distribution to the extent of the earnings and profits accumulated after February 28, 1913. On the other hand, a cancellation or redemption by a corporation of all of the stock of a particular shareholder, so that the shareholder ceases to be interested in the affairs of the corporation, does not effect a distribution of a taxable dividend. A bona fide distribution in complete cancellation or redemption of all of the stock of a corporation, or one of a series of bona fide distributions in complete cancellation or redemption of all of the stock of a corporation, is not essentially equivalent to the distribution of a taxable dividend. If a distribution is made pursuant to a corporate resolution reciting that the distribution is made in liquidation of the corporation, and the corporation is completely liquidated and dissolved within one year after the distribution, the distribution will not be considered essentially equivalent to the distribution of a taxable dividend; in all other cases the facts and circumstances should be reported to the Commissioner for his determination whether the distribution, or any part thereof, is essentially equivalent to the distribution of a taxable dividend.

S. Rep. No. 52, 69th Cong., 1st Sess., p. 15 (1939-1 Cum. Bull. (Part 2) 332, 344):

PARTIAL LIQUIDATION

Section 201 (g): It has been contended that under existing law a corporation, especially one which has only a few stockholders, might without resorting to the device of a stock dividend, be able to make a distribution to its stockholders which would have the same effect as a taxable dividend. For example: Assume that two men hold practically all the stock in a corporation, for which each had paid $50,000 in cash, and the corporation had accumulated a surplus of $50,000 above its cash capital. It is claimed that under existing law the corporation could buy from the stockholders, for cash, one-half of the stock held by them and cancel it without making the stockholders subject to any tax. Yet this action, in all essentials, would be the equivalent of a distribution through cash dividends of the earned surplus. The subdivision as rewritten by the House bill is intended to make clear that such a transaction is taxable and the committee approves the provision, which obviously does not apply in cases of complete liquidation of all the stock of the corporation.

The House bill provided that the amendment should be retroactive to January 1, 1925. The committee recommends that the provisions of the 1924 Act in this respect remain in effect during the calendar year 1925 and that the change in the law should become effective only as of January 1, 1926.

Rules of the United States Court of Appeals for the Ninth Circuit:

RULE 10

APPEALS, RETURN AND RECORD

1. In all cases on appeal or review, civil or criminal, the clerk of the trial court or commission shall transmit to the clerk of this court the original files designated by the respective parties as the record on appeal or review.

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RULE 17

PRINTING RECORDS

1. Records shall be printed under the supervision of the clerk of this court. Each party shall pay the estimated expense of printing the portions of the record he designates. * * *

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6. In all cases, including those on petition for review to enforce or to set aside an order of a United States Board or Commission, the appellant or petitioner, upon the filing of the record in this court, shall file with the clerk a concise statement of the points on which he intends to rely. With such statement the appellant or petitioner shall file a designation of all of the record which is material to the consideration of the appeal or review and forthwith serve on the adverse party a copy of the statement and designation. The adverse party, within 10 days thereafter, may designate in writing, filed with the clerk, additional parts of the record which he thinks material; and if he shall not do so, he shall be held to have consented to a hearing on the parts designated. If parts of the record shall be so designated by one or both of the parties, or if such parts be distinctly designated by stipulation of counsel for the respective parties, the clerk shall print those parts only; and the court will consider

nothing but those parts of the record and the points so stated. If at the hearing it shall appear that any material part of the record has not been printed, the appeal may be dismissed, or such other order made as the circumstances may appear to the court to require. If the appellee shall have caused unnecessary parts of the record to be printed, such order as to costs may be made as the court shall think proper.

All statements and stipulations filed hereunder shall distinctly and accurately refer to the pages of the original certified record as well as the documents to be printed or omitted.

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U. S. GOVERNMENT PRINTING OFFICE: 1933

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